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## SIGNIFICANT CHANGES IN PUBLIC UTILITY LAW

HUGH EVANDER WILLIS \*

THE TERM public utilities will be used here in the generic sense. The term is sometimes used in a specific sense to include such businesses as gas, electricity, telephone, telegraph, etc. This was at first the sole way in which the term was used. More recently the term has been extended to include all businesses affected with a public interest, or those which are otherwise designated as public callings. In this sense, the term will include innkeepers, railways, and other common carriers of goods and of passengers, public warehousemen, and the enterprises formerly designated as public utilities.

However, this discussion will be confined to changes which have affected the law of public utilities as a whole. It will not include changes in the law of specific public utilities. Great changes for example have been incorporated in the law as to the liability of innkeepers and of common carriers with reference to the safety of goods and to the termination of their common law liability. Such changes as these will not come within the range of our discussion which will be confined to more general tendencies.

The law of public utilities is not the only form of social control which has been applied to the businesses which are classified as public utilities. Besides the regulation of these businesses according to the law of public utilities, these businesses have also been regulated (1) by *laissez-faire*, or self-regulation instead of social control, (2) by the law of enforced competition, (3) by social control like the public utility trust of Great Britain, and (4) by government ownership and operation, or government ownership with private operation under contract, as a substitute for private ownership. *Laissez-faire* was the rule in the United States for the most part prior to 1875. Enforced competition was cham-

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pioneered by President Woodrow Wilson<sup>1</sup> and is the theory embodied in the Clayton Act, Federal Trade Commission Act, and the Sherman Anti-trust Act and other anti-trust acts, in so far as they were made applicable to public utilities. The public utility trust of Great Britain has never been tried in the United States.<sup>2</sup> Government ownership of utilities has never had much trial in the United States until fairly recent times and even now it has not been tried extensively on any large scale. The T. V. A. experiment is probably the most significant form of government ownership that we have had in the United States. However, in colonial days there probably was not the antagonism to public ownership which manifested itself in the 19th century.

The law of public utilities is of very early origin after the Norman Conquest, but it has attained its greatest importance only in relatively recent times. During all of its history, it has been undergoing significant changes. In the strict period 1272-1613, the public utilities were common callings. These included all trades and businesses, although at that time these were not numerous.<sup>3</sup> All of the trades were liable for negligent acts in trade,<sup>4</sup> and bailees were liable as insurers for the safety of goods

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<sup>1</sup> WILSON, *NEW FREEDOM* (1913).

<sup>2</sup> The essential characteristics of this form of social control are as follows:

1. Monopoly (in each industry).
2. Elimination of the profit motive.
3. The elimination of voting stockholders and the replacement of directors by government appointed trustees.
4. The payment of fixed interest from 3% to 5%, and the making of stock not tax exempt.
5. The use of surplus and earnings to reduce charges or to reduce taxes by turning them into the treasury of government.
6. The establishment of business principles.
7. The appointment of the trustees by the government on the basis of public spirit and general ability rather than interest representation or party selection.
8. The placing of the business management in a general manager appointed by the trustees with all salaries fixed by law.
9. Making responsible for the scheme *ex officio*, the minister in charge of that government department most closely related to the industry.
10. The requirement of treasury approval before the floatation of additional securities.

Revised from: Dimock, *British and American Utilities* (1933) 1 U. OF CHI. L. REV. 265.

<sup>3</sup> Adler, *Business Jurisprudence* (1914) 28 HARV. L. REV. 135, 152, 158.

<sup>4</sup> Arterburn, *Origin and First Test of Public Callings* (1926) 75 U. OF PA. L. REV. 411, 419.

in their possession.<sup>5</sup> The only regular public utility duty which rested upon the common callings in the strict period was the duty to serve.<sup>6</sup> In the period of equity, 1613-1793, the public utilities did not include all businesses but only monopoly businesses. At least this was true so far as Lord Hale had influence on this part of the law.<sup>7</sup> To the duty to serve there was added in this period at least one other duty, the duty to serve for reasonable compensation.<sup>8</sup> In this period, the liability for the safety of goods was also somewhat modified. In the period of maturity, 1793-1875, two new public utility duties were added: the duty to serve with reasonably adequate facilities,<sup>9</sup> and the duty to serve without discrimination.<sup>10</sup> Prior to this time, there was no liability except under the law of negligence. But the most significant development of the law of public utilities in the period of maturity was the substitution of contract law for the law of public utilities. In accordance with the goal of law in the period of maturity, the parties were allowed to regulate their conduct for the most part by private contracts.<sup>11</sup>

With the period of socialization, 1875 to date, there came a revival of the law of public utilities. The courts, especially the United States Supreme Court, began to put limitations upon freedom of contract.<sup>12</sup> As a result of the Granger movement, there was a revulsion against the supplanting of the law of public callings by contract, and governmental regulation under the law of public callings again came into vogue.<sup>13</sup> In the celebrated case of *Munn v. Illinois*,<sup>14</sup> the United States Supreme Court gave a twist to the

<sup>5</sup> Southcote's Case, 4 Co. Rep. 836 (1601); *Morse v. Slue*, 1 Vent. 190, 2 Lev. 69 (1671).

<sup>6</sup> WILLIS, CONSTITUTIONAL LAW (1936) 760.

<sup>7</sup> Hale, *De Jure Maris*, 1 HARGRAVE TRACTS 6; Hale, *De Portibus Maris*, 1 HARGRAVE TRACTS 78.

<sup>8</sup> *Allnut v. Inglis*, 12 East 527 (K. B. 1810).

<sup>9</sup> *Bremner v. Williams*, 1 C. & P. 414 (N. P. 1824); *Shepard v. Milwaukee Gas Light Company*, 6 Wis. 539 (1858).

<sup>10</sup> *Scofield v. Railway Co.*, 43 Ohio St. 571 (1885).

<sup>11</sup> *Judson v. Western R. R. Corp.*, 6 Allen 486 (Mass. 1863).

<sup>12</sup> *Railroad Co. v. Lockwood*, 17 Wall. 357 (U. S. 1873); *Express Co. v. Caldwell*, 21 Wall. 264 (U. S. 1874).

<sup>13</sup> *Munn v. Illinois*, 94 U. S. 113 (1876).

<sup>14</sup> The reestablishment of the law of public utilities involved a question of due process. As to this point the Court based its decision on the fact that this social control had been a part of English common law and that our Constitution had been adopted in the light of this practice. It might have held it due process of law because of the need for the protection of the social interest both in the general economic progress and in the individual life.

The Court held that it was not a violation of the equality clause to make this social control apply simply to businesses classed as public utilities

law of public utilities as it had been announced by Lord Hale with reference to wharves, so as to make it apply to every business which might be classed as a public utility. This was a use of Lord Hale's law which must have made him twist in his grave.<sup>15</sup> Since this time, though public utilities and their patrons have been permitted to make contracts to govern their relations, social control has very largely controlled the terms of those contracts and has limited them by the law of public utilities as it has now developed. In this period of socialization one new duty, that of continuity, has apparently developed.<sup>16</sup>

This paper will be concerned for the most part with those significant changes in public utility law in the United States which have occurred since 1875, or during the period of socialization.

### TEST FOR PUBLIC UTILITIES

One significant change in public utility law which has occurred since the decision of *Munn v. Illinois* has been the change in the test for public utilities. The test adopted in this case was the test of virtual monopoly, suggested by Lord Hale. The test as to what businesses shall be and what shall not be classed as public utilities is important because, if a business is classed as a public utility, there is a large body of public utility law which applies to it; if it is not a public utility, this body of law will not apply to it, or at least it has not been applied to it until very recently. When the Supreme Court, therefore, adopted the test of virtual monopoly as the test for public utilities, it thereby subjected all of the businesses which are virtual monopolies to the social control known as public utility law. The United States Supreme Court decisions have been the most important in determining the test for public utilities in the United States. State decisions have not always agreed on the test of public utilities, but in the long run, they have tended to follow the test adopted by the Supreme Court. The Court seemed to put a limitation on the test of virtual monopoly in the case of *Budd v. New York*.<sup>17</sup> But, with this

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because there was a sufficient reason for this classification in the fact that businesses of this sort needed a social control which no other businesses needed.

<sup>15</sup> McAllister, *Lord Hale and Business Affected with a Public Interest* (1930) 43 HARV. L. REV. 759.

<sup>16</sup> *Wilson v. New*, 243 U. S. 332 (1917); *Bullock v. Florida*, 254 U. S. 513 (1921); *Wolff Packing Company v. Court of Industrial Relations*, 262 U. S. 522 (1923); *St. Louis-San Francisco Ry. v. Alabama Public Service Comm.*, 279 U. S. 560 (1929).

<sup>17</sup> 143 U. S. 517 (1892).

exception, the test of virtual monopoly continued to be the test until the decision of *Brass v. North Dakota*.<sup>18</sup>

The Supreme Court in the last case seemed almost to abandon the test of virtual monopoly and to permit a legislative declaration to make any business a public utility. In *German Alliance Insurance Co. v. Lewis*<sup>19</sup> the Supreme Court adopted a test which was two-fold in nature, virtual monopoly and indispensable service, a test which had been suggested in the case of *Budd v. New York*; but the Court did not directly overrule the case of *Brass v. North Dakota*. However in *Wolff Packing Co. v. Court of Industrial Relations*<sup>20</sup> the Supreme Court directly overruled *Brass v. North Dakota*, held that a business could not be made a public utility by legislative declaration, and adopted a three fold test for public utilities: (1) a grant of privilege, (2) historical survival, and (3) virtual monopoly and indispensable service. The third part of the test is the one which had been emerging in the prior cases and is the only one of importance so far as new businesses are concerned and perhaps it is sufficient to take care of the classes for which the court suggested the first two parts of the test. This test has been consistently applied in cases decided since the *Wolff Packing Company Case*.<sup>21</sup>

In spite of the fact that since the decision of *Munn v. Illinois* the test of a public utility has been made narrower, the number of public utilities has been made larger; and, therefore, the scope of the law of public utilities has been made broader. This, perhaps, has been due to the fact that businesses have changed, so that there are more virtual monopolies now than formerly; and economic and social conditions have changed, so that there are more indispensable services now than there were at one time. All along through the years, more and more businesses have been

<sup>18</sup> 153 U. S. 391 (1894).

<sup>19</sup> 233 U. S. 389 (1914). Followed by *Block v. Hirsh*, 256 U. S. 135 (1921).

<sup>20</sup> 262 U. S. 522, 538 (1923). The language of the Court was, "... the indispensable nature of the service and the exorbitant charge and arbitrary control to which the public might be subjected without regulation [because of 'monopoly']."

<sup>21</sup> *Tyson v. Banton*, 273 U. S. 418 (1927) (theaters, not an indispensable service); *Ribnik v. McBride*, 277 U. S. 350 (1928) (employment agencies, not an indispensable service); *Williams v. Standard Oil Co.*, 278 U. S. 235 (1929) (selling gasoline, not a monopoly); *Tagg Brothers v. United States*, 280 U. S. 420 (1930) (commission men, both indispensable service and virtual monopoly); *O'Gorman and Young v. Hartford Fire Ins. Co.*, 282 U. S. 251 (1931) (insurance, a public utility); *New State Ice Co. v. Liebmann*, 285 U. S. 262 (1932) (manufacturing and selling ice, not an indispensable service).

put into the class of public utilities and there are now new businesses which would undoubtedly be so classified under the test as it now stands if the question was presented to the United States Supreme Court. Among such businesses might be named aviation, radio and holding companies of public utilities.<sup>22</sup>

### PUBLIC UTILITY DUTIES

Another significant change in public utility law during the period of socialization has been the growth of public utility duties and changes in old public utility duties. Most of the growth in this part of public utility law occurred before the period of socialization and we have already referred to that. We have also called attention to the fact that the duty of continuity is a new duty which has arisen in the period of socialization.<sup>23</sup> Changes in the duty to serve all, the duty to serve with reasonably adequate facilities, the duty to serve without discrimination and the duty to serve for reasonable compensation have occurred as the Court has applied this law to new and ever changing conditions.

For example the duty to furnish reasonably adequate facilities now requires railways to equip their cars with vestibule doors although at one time this could not have been required.<sup>24</sup> In the same way, railways may now be required to equip their trains with power brakes,<sup>25</sup> to build union stations,<sup>26</sup> and to furnish seats

<sup>22</sup> WILLIS, CONSTITUTIONAL LAW (1936) 765. For general discussions of the test of public callings see: FREUND, POLICE POWER, 23, 388; WYMAN, PUBLIC SERVICE CORPORATIONS § 156. Boudin, *Is Economic Planning Constitutional?* (1933) GEORGETOWN LAW JOURNAL 253, 387; Adler, *Business Jurisprudence* (1914) 28 HARV. L. REV. 135, 152; Arterburn, *Origin and First Test of Public Callings* (1927) 75 U. OF PA. L. REV. 411, 419; Berman, *Present Status of the Kansas System of Compulsory Arbitration* (1928) 23 ILL. L. REV. 30; Burdick, *Origin of the Peculiar Duties of Public Service Companies* (1911) 11 COL. L. REV. 514, 522; Hardman, *Public Utilities* (1931) 37 W. VA. L. Q. 250; Robinson, *The Public Utility: A Problem in Social Engineering* (1928) 14 CORN. L. Q. 1; Robinson, *Public Utility Concept* (1928) 41 HARV. L. REV. 277; Simpson, *Due Process and Coal Price Regulation* (1924) 9 IOWA L. BULL. 145; Willis, *When Is a Business Affected with a Public Interest?* (1928) 3 IND. L. J. 384. Public Utility Holding Company Act, 49 STAT. 803, 15 U. S. C. A. § 879 (Supp. 1936).

<sup>23</sup> This is not an absolute duty, but public utilities (at least most of them) cannot discontinue their systems without first obtaining either commission consent or a judicial determination of fact that an entire system can operate only at a loss. *Brooks-Scanlon Co. v. Railroad Comm.*, 251 U. S. 396 (1920); *Bullock v. Florida*, 254 U. S. 513 (1921); *Ft. Smith Light and Traction Co. v. Bourland*, 267 U. S. 330 (1925).

<sup>24</sup> 10 C. J. 961.

<sup>25</sup> *Fairport Painesville & Eastern R. R. v. Meredith*, 292 U. S. 589 (1934).

<sup>26</sup> *Atchison T. & S. F. R. R. v. Railroad Comm.*, 283 U. S. 380 (1931).

to passengers.<sup>27</sup> Telephone companies also may be required to furnish physical connections.<sup>28</sup> The duty to serve without discrimination has been limited in application until now segregation of the races is permitted either in inns or on railways.<sup>29</sup> Even the oldest duty to serve all has been explained and qualified so as to exclude from it persons fleeing from justice, afflicted with contagious diseases, planning to gamble on trains or otherwise to endanger the comfort and safety of passengers.<sup>30</sup>

The changes in the duty to serve for reasonable compensation have recently been so great that they are entitled to a little more detailed consideration. In order to determine when a public utility is receiving reasonable compensation some basis for such determination must be adopted. Any basis would involve both a rate base (valuation) and a rate of return. The decisions of the United States Supreme Court on these subjects have neither been consistent nor clarifying, but they have worked significant changes in the application of the law of public utilities.

#### BASE RATE

The rate base for the determination of reasonable compensation for public utilities might be determined in any one of a number of different ways which have been suggested. One such way would be original capitalization. This way has been definitely rejected because of the watering of stock in the past. Another way would be by the value assessed for taxation. But the purpose here is so different that this method has not received much consideration. The first method adopted by the Supreme Court for determining the rate base was that of fair value. This was the rate base adopted in the case of *Smyth v. Ames*.<sup>31</sup> In this rate base, consideration is given to a congeries of diverse and mutually exclusive elements, such as original cost, amount of permanent improvements, value of bonds and stocks, present cost, earning capacity and operating expenses. To attempt to determine a rate base in this way is to attempt the impossible. Justice Brandeis, in his dissent, has conclusively pointed out that "Obviously 'value'

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<sup>27</sup> *Camden & Atlantic R. R. v. Hoosey*, 99 Pa. 492 (1882).

<sup>28</sup> *McCardle v. Akron Telephone Co.*, 87 Ind. App. 59, 160 N. E. 48 (1928).

<sup>29</sup> *BEALE, INNKEEPERS AND HOTELS* § 55; *Chicago & N. W. Ry. v. Williams*, 55 Ill. 185 (1870).

<sup>30</sup> *Thurston v. Union Pacific R. R.*, 23 Fed. Cas. No. 14,019 (C. C. D. Neb. 1877).

<sup>31</sup> 169 U. S. 466 (1898).



cannot be a composite of all of these elements." <sup>32</sup> Yet in spite of this fact, the Supreme Court has continued to adhere to fair value as its rate base for determining reasonable compensation. <sup>33</sup>

In the case of *McCardle v. Indianapolis Water Company* <sup>34</sup> the Court adopted reproduction cost as the rate base for determining reasonable compensation. The cases following *Smyth v. Ames* had been giving increasing weight to the importance of reproduction cost and finally in the *McCardle Case* this was adopted as the sole element to be considered. But in the *St. Louis & O'Fallon Railway Case* <sup>35</sup> the Court evidently came to the conclusion that it had gone too far in the *McCardle Case*, and, not knowing what else to do, fell back again on the amorphous fair value rate base of *Smyth v. Ames*. Yet the Court still continues to give chief emphasis to reproduction cost and in the case of *United Railways and Electric Company v. West* <sup>36</sup> held that since the rate base requires figuring according to present value, depreciation must be figured in the same way. Reproduction cost as a rate base is likely to be unfair because too large after a period of inflation and too small after a period of deflation; and uncertain because it depends, for the most part, on imaginative guessing by engineers. For this reason another rate base called prudent investment, which is the original cost corrected so as to eliminate any elements which are not just and fair, has been suggested as the best rate base for the determination of reasonable compensation. This was set forth by Justice Brandeis in a dissenting opinion in *Missouri v. Public Service Commission* <sup>37</sup> and has been followed by some state courts. But the Supreme Court has not as yet adopted it though it is taking a more realistic approach towards the subject. <sup>38</sup> The Supreme Court evidently has not as yet decided upon any final rate base, but it cannot forever wallow in the uncertainties of the rate base announced in *Smyth v. Ames*. <sup>39</sup>

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<sup>32</sup> *Missouri v. Public Service Comm.* (Southwestern Bell Case) 262 U. S. 276, 295 (1923).

<sup>33</sup> *Minnesota Rate Cases*, 230 U. S. 352 (1913); *Southwestern Bell Case*, 262 U. S. 276 (1923); *Georgia Ry. & Power Co. v. Railroad Comm.*, 262 U. S. 625 (1923); *Bluefield Water Works and Improvement Co. v. Public Service Comm.*, 262 U. S. 679 (1923).

<sup>34</sup> 272 U. S. 400 (1926).

<sup>35</sup> *St. Louis & O'Fallon Ry. Co. v. United States*, 279 U. S. 461 (1929).

<sup>36</sup> 280 U. S. 234 (1930); *Los Angeles Gas & Electric Corp. v. Railroad Comm.*, 289 U. S. 287 (1933).

<sup>37</sup> 262 U. S. 276, 289 (1923).

<sup>38</sup> *Lindheimer v. Illinois Bell Tel. Co.*, 292 U. S. 151 (1934); *Dayton Power & Light Co. v. Public Utilities Comm.*, 292 U. S. 290 (1934).

<sup>39</sup> Dorety, *Functioning of Reproduction Cost in Public Utilities and Rate Making Valuation* (1923) 37 HARV. L. REV. 173; Edgerton, *Value of the*

## THE RATE OF RETURN

At first the United States Supreme Court was inclined to allow about six per cent as the rate of return.<sup>40</sup> Later it held that six per cent was too low a rate of return.<sup>41</sup> Finally it allowed a rate of return as high as eight per cent when over two-thirds of the money invested in the business was borrowed money, borrowed at a rate much lower than this.<sup>42</sup> In *Los Angeles Gas and Electric Corp. v. Railroad Commission*<sup>43</sup> a rate of seven per cent was allowed.

The duty to serve for reasonable compensation which rests upon public utilities is supposed to limit the amount of their profits to less rather than to increase their profits to more than other businesses obtain. Yet the rate of return guaranteed to public utilities by the United States Supreme Court has probably given these businesses affected with a public interest a right to more profits than other businesses, on the average, have been able to obtain. The Supreme Court has said that public utilities are entitled to the same sort of return that is obtained where money is invested in other equally secure enterprises. The United States government has been able to sell its tax exempt securities for from two to four per cent interest. Insurance companies and savings banks have allowed a lower rate of interest than this on money invested with them. Large corporations, both public utilities and those not public utilities, have been able to sell their bonds not tax exempt for an interest rate of four per cent to

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*Service as a Factor in Rate-Making* (1919) 32 HARV. L. REV. 516; Goddard, *Public Utility Valuation* (1917) 15 MICH. L. REV. 206; Guernsey, *Value in Confiscation Cases* (1929) 77 U. OF PA. L. REV. 575; Hale, *The "Physical Value" Fallacy in Rate Cases* (1921) 30 YALE L. J. 710; Hardman, *Recent Developments in Regard to Rate Regulation* (1923) 30 W. VA. L. Q. 70; Henderson, *Railway Valuation and the Courts* (1920) 33 HARV. L. REV. 902, 1031; Howell, *Recent Developments in the Application of the Rule of Smyth v. Ames* (1925) 3 TEX. L. REV. 412, Richberg, *The Supreme Court Discusses Value* (1924) 37 HARV. L. REV. 289; Richberg, *A Permanent Basis for Rate Regulation* (1922) 31 YALE L. J. 263; Robinson, *Duty of a Public Utility to Serve at Reasonable Rates: The "Valuation" War* (1926) 6 N. C. L. REV. 243; Whitten, *Fair Value for Rate Purposes* (1914) 27 HARV. L. REV. 419; Notes (1927) 3 IND. L. J. 225; (1925) 24 MICH. L. REV. 166.

<sup>40</sup> *Willcox v. Consolidated Gas Company*, 212 U. S. 19 (1909); *Des Moines Gas Co. v. Des Moines*, 238 U. S. 153 (1915).

<sup>41</sup> *Bluefield Water Works and Improvement Co. v. Public Service Comm.*, 262 U. S. 679 (1923); cf. *Dayton-Goose Creek Ry. Co. v. United States*, 263 U. S. 456 (1924).

<sup>42</sup> *United Railways and Electric Co. of Baltimore v. West*, 280 U. S. 234 (1930).

<sup>43</sup> 289 U. S. 287 (1933).

five per cent and their preferred stock for six per cent. Public utilities are some of the biggest and safest businesses in the United States and they would have been even safer if they had not been allowed as high a rate as has been guaranteed them. The Court has evidently allowed increasingly too high a rate of return.

The result on the one hand of such a high rate of return as the Supreme Court has allowed has been to prevent the economic development both of the public utilities and of the country as a whole. High freight and passenger rates for the railroads, instead of making them prosperous, were tending to injure them, because with such high rates they could not meet other competition. It was only when the Interstate Commerce Commission forced lower rates upon the railroads that they began to make more money. High rates in the same way hindered development of electric companies. The companies which made the greatest profits during the year 1936 were those which had been forced to cut their rates by the T. V. A. The worst effect of these high rates has, however, been the retarding of the economic development of the country as a whole. The high electric rates were robbing our country of cheap electricity. No one can estimate the loss to our country as a whole in not having cheap electricity.

The result on the other hand of this high rate of return has been the encouragement of an orgy of high finance which has been bad both for the public utilities and for the public as a whole. The Supreme Court has allowed a rate of return higher than the dividends which public utilities have had to pay on preferred stock and the interest which they have had to pay on bonds. In order to absorb this difference and to cover up this fact, public utility magnates have organized holding companies to own the common stock of the operating companies and they have financed the holding companies in the same way that the operating companies had been financed by selling bonds and preferred stock for less than the rate of return guaranteed public utilities by the Supreme Court. Then one holding company has been pyramided upon another. In this way a few insiders have been obtaining returns running all the way from twenty per cent to one thousand per cent.<sup>44</sup> This was bad enough, but they were not content merely to exploit the situation created by the United States Supreme Court. They were so anxious to indulge in high finance that they indulged in such sorts of scandals, corruptions and wild-cat

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<sup>44</sup> WILLIS, *CONSTITUTIONAL LAW* (1936) 775, 782. Cohen, *Confiscatory Rates and Modern Finance* (1929) 39 YALE L. J. 151.

speculations that very frequently they not only lost the exorbitant profits they might otherwise have obtained but they brought their businesses down in ruins upon their heads.

So far as concerns the duty of public utilities to serve for reasonable compensation, therefore, the law of public utilities, or governmental regulation has not been a success. So far as concerns the other public utility duties, probably the law of public utilities has on the whole been fairly successful. But the failure of public utility law in the matter of reasonable compensation has been so great that it is a question of whether all the law of public utilities should not be abandoned and some other scheme of social control tried in its stead. The reason for this failure has been three fold. First, it has been due to the attitude of public utilities who have fought governmental regulation and have tried to make it ineffective. Second, it has been due to the administration of the law by state public service commissions who have sometimes been subject to corruption by public utilities, and frequently filled by men who lack qualifications for their task. Third, it has been due to the unfortunate decisions of the United States Supreme Court on the rate base and the rate of return for the determination of reasonable compensation. These decisions have probably been responsible more than any other cause for the failure of governmental regulation of public utilities.

More recently a slight attempt on the part of the federal government has been made to correct the evils of public utility holding companies. The United States Supreme Court has taken the position that in determining the reasonableness of the income allowed to an operating company, the amount paid by an operating company to a holding company may be investigated.<sup>45</sup> Congress also has passed a public utility holding company act which puts important limitations upon such interstate holding companies.<sup>46</sup> While it does not abolish holding companies in the public utility field, it requires registration for interstate commerce and for use of the United States mails, makes it unlawful even for registered companies to issue or sell securities from house-to-house without a declaration filed and forbids the acquirement of other securities without consent of the Securities and Exchange Commission, simplifies the holding company systems so as to eliminate pyramiding, forbids service, sales and construction con-

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<sup>45</sup> *Smith v. Illinois Bell Tel. Co.*, 282 U. S. 133 (1930); *Western Distributing Co. v. Public Service Comm. of Kansas*, 285 U. S. 119 (1932).

<sup>46</sup> *Public Utility Holding Company Act*, 49 STAT. 803, 15 U. S. C. A. § 79 (Supp. 1936); *Notes*, (1936) 16 B. U. L. REV. 178; (1936) 4 GEO. WASH. L. REV. 532; (1935) 45 YALE L. J. 468.

tracts for operating companies and makes profits acquired by officers inure to holding companies. This act raises some important constitutional questions. One is a question of violation of our dual form of government, but probably the act can be upheld here under the commerce power and the postal power. Another is a question of delegation of legislative power, but probably sufficient standards for the Security and Exchange Commission have been set up to meet this point. A third constitutional question involves due process, but it would seem that there is a sufficient social interest to be protected to make the act constitutional so far as concerns this point, either under the police power or under the regulation of public utilities. If the act is constitutional, it will contribute in no small measure to the elimination of some of the evils which have grown up in this particular field of governmental regulation.

However, the regulation of holding companies will not solve the main problem of governmental regulation of public utilities. That problem can only be solved by a change in the law as to the rate base and as to the rate of return. A change in the law as to the rate of return is perhaps the most important thing. It would seem to the writer that an experimental rate of return of four per cent would come as near to being the correct rate as any that might be suggested. This rate is as high as the rates of return which can be found in other comparable investments, and under the public utility trust of Great Britain. It is believed that if a rate no higher than this was allowed, there would be no difficulty in public utilities obtaining all the money which they need for their enterprises. When they are able to sell their bonds for from four per cent to five per cent interest it seems very singular that the companies should be guaranteed a higher rate of return than they have to pay when they borrow money. If this rate of return was all that was allowed, it would automatically eliminate holding companies and most of the other evils of high finance which have crept into the public utility business, but the reform waits upon the Supreme Court. Until the Supreme Court reverses its decisions on this point, it would seem no effective solution of many public utility problems is possible.

#### PUBLIC COUNSELLOR

A development in public utility law of some significance is the creation of the office of public counsellor. Many states have now created this office. The reason for the creation of public counsellors has been the failure on the part of public service commissions

to aid the legislatures in the development of policies and to apply administrative control to public utilities, and their attempt to act more or less as courts in deciding conflicting claims according to law. In the beginning it was assumed that the courts were adequate to protect the public utilities and that public service commissions had, as their function, the protection of the public. Yet more and more they have tended to become quasi-judicial bodies. This has been due partly to the personnel of the commissions (generally lawyers familiar with regular legal procedure) and to the attitude of the courts in commission cases.<sup>47</sup> The office of public counsellor has been established to represent the public in litigation before public service commissions.<sup>48</sup>

#### EXTENSION OF PUBLIC UTILITY LAW TO OTHER BUSINESSES

A most significant recent development of public utility law has been the extension of this law so far as it concerns the regulation of prices to other businesses than public utilities. In the case of *Stephenson v. Binford*,<sup>49</sup> the Supreme Court upheld the regulation of the charges of contract carriers. This seemed to be an extension of public utility law to other businesses rather than an enlargement of the number of public utility businesses but if there was any doubt on the subject, this was removed by two other cases. In *O'Gorman & Young v. Hartford Fire Ins. Co.*,<sup>50</sup> the Supreme Court permitted the regulation of the charges of insurance brokers. This, of course, was a price regulation of a public utility business but in the prior case of *Wolff Packing Co. v. Court of Industrial Relations of Kansas*,<sup>51</sup> the Supreme Court had held that it would not allow the fixing of wages of employees even if they were working for public utilities. In the case of *Nebbia v. New York*,<sup>52</sup> the Supreme Court definitely applied a public utility duty to a business which was not a public utility. In the *Nebbia Case* the Supreme Court held that the prices in a milk business could be regulated even though the business did not have a virtual monopoly so that it could be declared a public utility. In the prior case of *Williams v. Standard Oil Co.*,<sup>53</sup> the Supreme Court had held that price fixing was illegal outside of

<sup>47</sup> *In re Northwestern Indiana Tel. Co.*, 201 Ind. 667, 171 N. E. 65 (1930).

<sup>48</sup> Cunningham, *Why a People's Counsel?* (May 29, 1930) 5 P. U. FOR. 676.

<sup>49</sup> 287 U. S. 251 (1932).

<sup>50</sup> 282 U. S. 251 (1931).

<sup>51</sup> 262 U. S. 522 (1923).

<sup>52</sup> 291 U. S. 502 (1934).

<sup>53</sup> 278 U. S. 235 (1929).

public utilities. This shows the significance of the change in the law of governmental regulation. The *Nebbia Case*, if taken at its face value, not only broke the United States taboo against price fixing, but opened the door to the extension of the social control, known as the law of public utilities, to all businesses and not simply to those which have a virtual monopoly and are rendering an indispensable service. Of course, as yet the Supreme Court has only extended the duty to serve for reasonable compensation to these other businesses, but it would not be surprising if, in the course of time, it extended all other of the duties. Civil rights statutes, as a matter of fact, have already required to serve without discrimination, businesses which are not public utilities such as barbers,<sup>54</sup> restaurants,<sup>55</sup> theaters,<sup>56</sup> and dance halls.<sup>57</sup> And these statutes have been upheld as proper exercises of the police power. The Supreme Court now seems inclined to take the position that the term "affected with a public interest means no more than that an industry, for adequate reason, is subject to control for the public good."

Stimulated by this development in the law, Congress has passed the Robinson-Patman Act <sup>58</sup> forbidding price discrimination between competing purchasers of goods of like grade and quality, if the goods are articles of interstate commerce, for use in the United States, and the discrimination tends to lessen competition and so create a monopoly. The wisdom of this legislation may be a matter of doubt but there is no doubt that Congress is undertaking to take advantage of the *Nebbia Case* to regulate prices outside of public utilities. It is founded on the *Nebbia Case*. It is an attempt to apply generally public utility law as to discrimination.

The administration of the Robinson-Patman Act has been committed to the Federal Trade Commission. The act does not forbid discrimination where there is a difference in cost of manufacture, sale or delivery. Prices may also change with the market. It does not forbid people to choose their own customers. But proof of discrimination creates a prima facie case and the Federal Trade Commission is authorized to issue a cease and desist order

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<sup>54</sup> *Messenger v. State*, 25 Neb. 674, 41 N. W. 638 (1889).

<sup>55</sup> *Ferguson v. Gies*, 82 Mich. 358, 46 N. W. 718 (1890).

<sup>56</sup> *Pickett v. Kuchan*, 323 Ill. 138, 153 N. E. 667 (1926); *Joyner v. Moore-Wiggins Co.*, 152 App. Div. 266, 269, 136 N. Y. Supp. 578 (4th Dep't 1912).

<sup>57</sup> *Johnson v. Auburn & Syracuse Elec. R. R.*, 222 N. Y. 443, 119 N. E. 72 (1918).

<sup>58</sup> 49 STAT. 1526, 15 U. S. C. A. § 13, 13a, 13b, 21a (Supp. 1936); Notes, (1936) 50 HARV. L. REV. 106; (1936) 70 U. S. L. REV. 620.

unless the accused shows justification. Brokerage commissions are not permitted as discounts. Advertising allowances are prohibited unless competitors use them. Discrimination between purchasers for resale is prohibited. It is made unlawful knowingly to induce or receive a discrimination in price. It relies upon the previous enforcement provisions of the Clayton Act but adds new criminal provisions and protects cooperative associations.

This act raises some difficult constitutional questions. Perhaps the *Nebbia Case* covers the extension of the law as to discrimination to fields outside of public utilities, though it probably is not safe to generalize much from the *Nebbia Case*,<sup>59</sup> but there are other constitutional questions. Probably the act as a whole could be upheld as constitutional if the Supreme Court will take the position that the prohibitions are not absolute. For the Federal Government to have the power indicated, it must be found in the commerce clause. The act is not expressly so limited but the Court could undoubtedly confine it to interstate commerce. So far as concerns due process, the Court could probably find a sufficient social interest for this regulation as much as it can for the regulation of public utilities, except for the *prima facie* rule. The Supreme Court has held that it is a denial of due process of law to make conclusive presumptions as to substantive consequences.<sup>60</sup> To uphold the act, it will have to hold that there is both a rational connection between the fact proved and the ultimate fact presumed, and that the inference of the latter fact is reasonable. The act seems to be aimed at chain stores. Whether or not it is a violation of the equality clause for this reason will depend upon whether or not the Supreme Court thinks the protection of independent wholesalers and retailers is sufficient reason for the classification.

#### JUDICIAL REVIEW

A still further significant change in public utility law concerns judicial view. In the case of *Munn v. Illinois*<sup>61</sup> the Supreme Court took the position that rate regulation was a legislative matter not subject to judicial view. But after the eighties, when due process was extended to matters of substance, the Court took the position that a due process question is involved in rate making and that if rates are too low, *i. e.*, confiscatory, public utilities are deprived of their property without due process of

<sup>59</sup> *Old Dearborn Distributing Co. v. Seagram-Distributing Corp.*, 299 U. S. 183, 190, 191 (1936).

<sup>60</sup> *Manley v. Georgia*, 279 U. S. 1. (1929).

<sup>61</sup> 94 U. S. 113 (1876).



law.<sup>62</sup> Of course, this made the question a judicial question and made the judicial power extend thereto.<sup>63</sup> This jurisdiction might have been limited to questions of law. The Supreme Court, however, in administrative cases extended judicial review not only to matters of fact<sup>64</sup> but to a trial *de novo*;<sup>65</sup> and held that if a court acts as an administrative agency, a judicial review by another court is necessary to satisfy the requirements of the law.<sup>66</sup> Recently the Court has begun to show more respect for commission findings of fact.<sup>67</sup> But it is doubtful if a satisfactory result can ever be obtained without abolishing judicial review in the case of due process as to matters of substance. Since there is no hope of this change coming to pass even by a change in the personnel of the Court, there seems necessary an amendment to the Constitution providing that the judicial power of the Courts of the United States shall not extend to due process as a matter of substance. Even then the judicial power would continue to extend to due process as a matter of procedure and would limit the methods of commissions.

#### GOVERNMENT OWNERSHIP

Government ownership is still another significant change or development in the field of public utilities. It is not a change in public utility law. It is a change in the solution of the problem of rendering indispensable social services where there is a situation of virtual monopoly. When government ownership comes in, private ownership and operation under the law of public utilities is likely to go out. There has been considerable development in the United States as well as in foreign countries in government ownership and operation of many social services. The T. V. A. experiment is one of the latest and perhaps one of the most successful of these experiments in the United States. Whether this is to develop into a scheme of government ownership and operation of important electrical services or whether it is to remain merely a yardstick for determining what is reasonable compensation for public utilities remains as yet an open

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<sup>62</sup> *Chicago M. & St. P. Ry. Co. v. Minnesota*, 134 U. S. 418 (1890); *Reagan v. Farmers' Loan & Trust Co.*, 154 U. S. 362 (1894).

<sup>63</sup> WILLIS, *CONSTITUTIONAL LAW* (1936) 668-672.

<sup>64</sup> *Ohio Valley Water Co. v. Ben Avon Borough*, 253 U. S. 287 (1920).

<sup>65</sup> *Crowell v. Benson*, 285 U. S. 22, 60 (1932).

<sup>66</sup> *Prentis v. Atlantic Coast Line Co.*, 211 U. S. 210 (1908).

<sup>67</sup> *Interstate Commerce Comm. v. New York, N. H. & H. R. R.*, 287 U. S. 178 (1932); *Florida v. United States*, 292 U. S. 1 (1934); *American T. & T. Co. v. United States*, 299 U. S. 232 (1936).

question. It, of course, is an attempt, so far as it is a yardstick, to accomplish indirectly what cannot be accomplished directly because of the barrier of United States Supreme Court decisions.

It now seems as though some other changes in public utility law must be made which will perhaps be more significant than any that have occurred in the last fifty or sixty years. Governmental regulation under the law of public utilities has not been a success for the reasons which we have already set forth. Something must be done about this. It is impossible to go back to a reign of *laissez-faire*. It is impossible to enforce competition. It probably would be impossible to introduce into the United States the public utility trust of Great Britain despite its many fine features. Government ownership and operation would probably solve the problem and accomplish the results desired; but in the United States, there is a great deal of prejudice against a general scheme of government ownership, in spite of the fact that we already have government ownership of about one-tenth of the business enterprises of the country. There remains, therefore, only private ownership and operation of public utilities under governmental regulation. Since the latter is not working satisfactorily, it cannot be continued longer without reformation. If the right reforms were instituted, this might become both an effective and fair scheme of social control. Apparently the only constitutional way to affect these reforms is by a reversal of its decisions on the rate of return and rate base by the United States Supreme Court. The Supreme Court recently has shown that it is coming closer to economic realities,<sup>68</sup> but it has not as yet given much ground for optimism on this point. However, if the reforms suggested were brought to pass, it would make the law of public utilities both a good scheme of social control for the field of public utilities and a good scheme of social control to incorporate into the general body of police power law, if it should seem wise to extend the scope of public utility law to all businesses.

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<sup>68</sup> *Lindheimer v. Illinois Bell Tel. Co.*, 292 U. S. 151 (1934).